

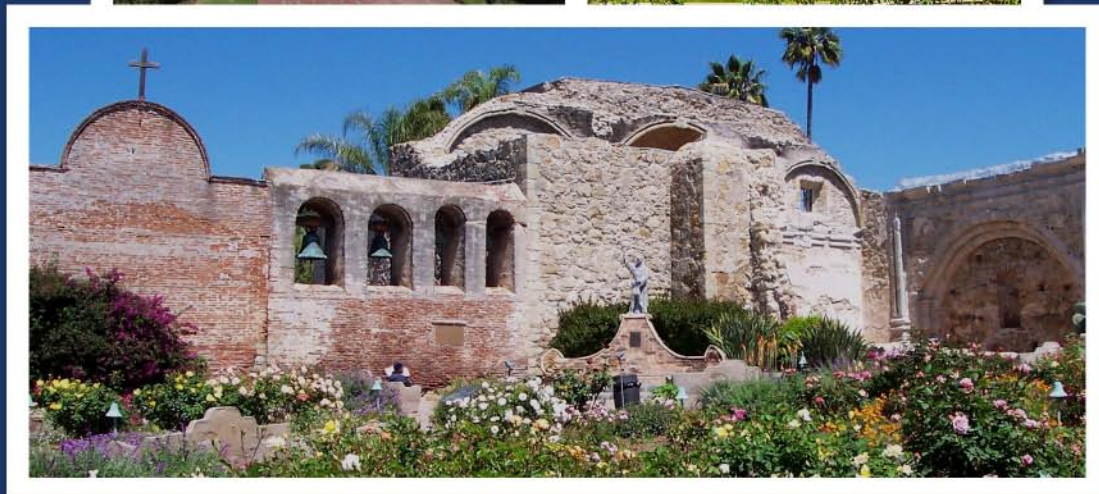
OC Board of Supervisors'
Internal Audit Department

O R A N G E C O U N T Y

INTERNAL AUDITOR'S ANNUAL REPORT

FOR FISCAL YEAR ENDING JUNE 30, 2011

DR. PETER HUGHES, CPA, CIA, CFE



OF ORANGE COUNTY

Contents

Our Organization, Our Performance

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ON THE COVER

The pictures on the front and back cover are provided courtesy of OC Community Resources/OC Parks. The photographs are landmarks that represent each supervisorial district as follows: First District – Bowers Museum, Second District – the larger photograph is of Huntington Beach Harbor (Front) and Bolsa Chica Wetlands (Back), Third District – Nixon Library, Fourth District – Angel Stadium, Fifth District – Mission at San Juan Capistrano.

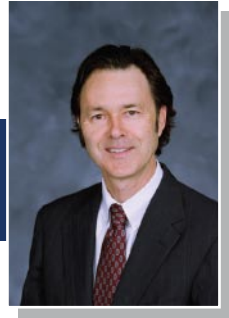
SPECIAL THANKS

The Internal Audit Department would like to thank the eGov team at the County Executive Office; specifically Mr. Stephen Salcido, Ms. Julie Nguyen and Ms. Grace Chou, for their insights, professional services, and graphics design support. The graphics design support and website maintenance provided is a valuable service. The professional support services we received from the eGov team helped us win the 2008 Bronze Website Award from the Association of Local Government Auditors.



A Message from

THE DIRECTOR OF INTERNAL AUDIT



Greetings,

We've had another productive year. We provided audit coverage, presence or services to **22 of 22 (100%) departments and agencies**. We completed **39 audits consisting of 36 Financial, Internal Control, Lease, and Information Technology Audits; 1 Control Self-Assessment & Process Improvement; and 2 Special Request Audits** directed by the Board of Supervisors (BOS) and the Audit Oversight Committee (AOC). We also completed **251 additional audit projects and activities** consisting of IT projects; fraud hotline alerts; risk analysis, technical assistance to County departments/agencies, cash losses, and other quality activities; and status and accountability reports to the BOS and AOC.

The **251 audit projects and activities** noted above include **36 quarterly and monthly reports to the BOS and AOC** and **1 Internal Audit Department Annual Report** that gives them timely and critical detailed information to act on in their decision-making process and to enable them to oversee the effectiveness of the Internal Audit Department. Also included are **49 IT Projects** consisting of monthly computer-assisted auditing (CAAT) reports of payroll and vendor payments, internal control assistance provided to new system implementations, and an **Audit Alert** to clarify working relationships with former employees. We performed our annual **Risk Assessment** in 22 departments and agencies, 5 Board Offices, and 1 comprehensive, countywide risk assessment for IT resulting in **2 Risk Assessments**. We monitored **18 Cash Losses** reported to the Auditor-Controller for consideration in our internal control audits. We provided **8 Technical Assistance Projects** to departments/agencies. We received **135 Fraud Hotline** allegations and issued **2 Fraud Hotline Reports** to the BOS and AOC.

This year we completed a demanding audit plan that included an audit of **Community Facilities Districts (CFDs) for Ladera Ranch** to determine if the special tax rates charged to the CFD residents were properly calculated and if bond proceeds were utilized as intended. As a result of our audit, the Mello Roos taxes for all 23 CFDs (6 for Ladera Ranch and 17 others) were **lowered nearly \$20 million over the next 3 years**. We also conducted an **Annual Compliance Audit of the Treasurer-Tax Collector** to ensure compliance in investment practices with CA Government Code requirements and an **Audit of the TTC's Cost Allocations to Pool Participants**.

We finished several audits of "core business processes" involving **Grants** (District Attorney); **Cash Disbursements** (Health Care Agency, OC Waste & Recycling); **County Fee Generating Revenue** (Health Care Agency, OC Waste & Recycling); **Countywide Fleet Management and Fuel Card Administration** (OC Public Works); **Contract Administration and Fiscal Monitoring** (Health Care Agency); **Revenue** (including contracted parking operations at OC Parks and John Wayne Airport); and **Revolving Funds** (County Counsel and Public Defender). We provided IT Internal Controls Assistance to several major system implementations including the CAPS+ HR/Payroll System, the Property Tax Management System (PTMS), and PA/PG's case management and financial system. We also started audits of the Sheriff-Coroner **Inmate Welfare Fund** and **Agreement with Immigrations and Customs and Enforcement (ICE)**, and an audit of the **Probation Department's Administration of Electronic Confinement/GPS programs and Health Care Agency Medical Billing Process**.

We develop our audit coverage to satisfy the need to provide "audit coverage" for all County departments on a biennial basis in accordance with CA Government Code 25250, and are pleased to report that our broad and diverse audit plan continues to fulfill this role.

The Governance Risk Compliance Group (GRC Group) selected OCIAD as their MVP in risk management for a government entity. We are very proud of this acknowledgement and will continue to provide the best possible "risk based" audit coverage of the internal controls over the County's business systems.

As in past years, we received full support and cooperation from all levels of County personnel and management in facilitating our audits and promptly addressing our audit concerns. It has been my pleasure to be of service to the OC Board of Supervisors in the County of Orange.

Sincerely,

Dr. Peter Hughes, CPA, CIA, CFE, CITP, CCEP, CFF
Director of Internal Audit

DR. PETER HUGHES

Director of Internal Audit
Ph.D., MBA, CPA, CIA, CFE,
CITP, CCEP, CFF

Find us at:
www.ocgov.com/audit

E-mail your comments to:
peter.hughes@iad.ocgov.com



■ THIS REPORT

This Internal Auditor's Annual Report to the Board of Supervisors is designed to provide the highlights and audit accomplishments of the audit activities during the past fiscal year. I am please to report we completed a very demanding Audit Plan in FY 10/11.

The governance and accountability established by the Board of Supervisors continues to ensure this department has the independence necessary to comply with all governmental and professional requirements.

The support role provided by internal auditing within any organization is expressed well by the following authoritative definition from the Institute of Internal Auditors:

“Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.”

In size of operations, the Orange County business environment is similar to large commercial firms and our annual budget would place Orange County in the Fortune 500. Orange County is the 6th largest county in the USA from over 3,100 counties. However, the County governmental environment is different from that of a typical commercial organization in a number of ways. The business diversity of the County's 25 separate departments is much more complex given our mandated and directed responsibilities. County executive management also has a public stewardship responsibility where all activities and reports have a concerned public audience as fund providers, recipients, and participants in this process.

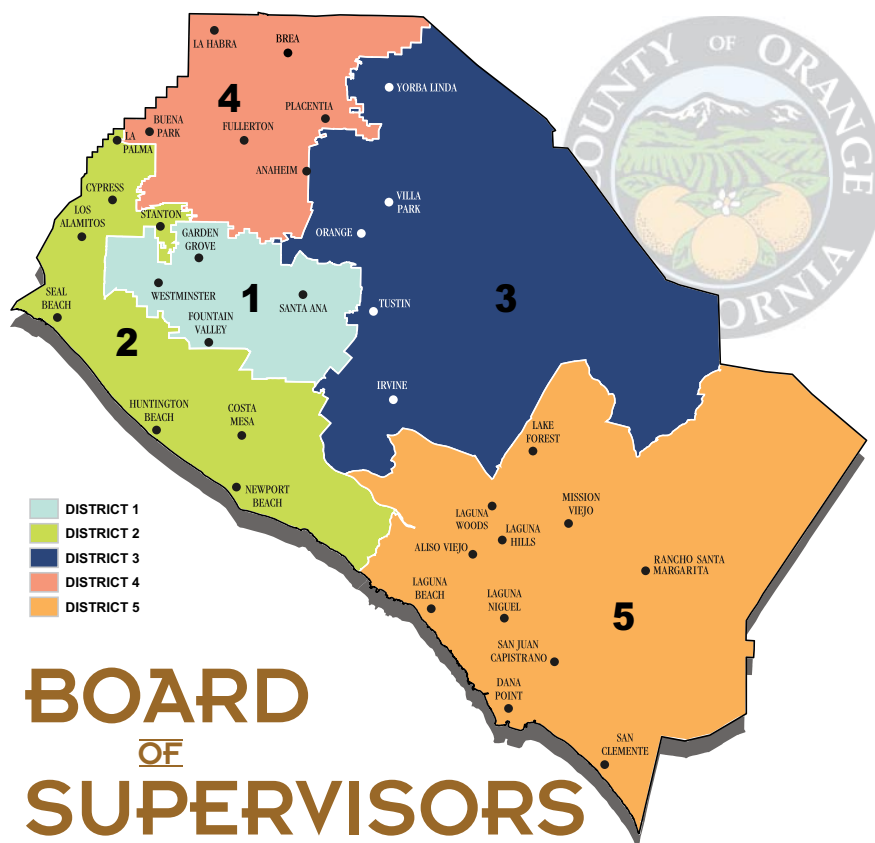
An important factor as to why the IAD functions so well is our organizational independence from the business units we audit within the County.



FY 2010/2011 INTERNAL AUDITOR'S ANNUAL REPORT



MEET OC'S BOARD OF SUPERVISORS



**Supervisor
Janet Nguyen**
First District

Fountain Valley (portions of), Garden Grove, Santa Ana, Westminister



**Vice Chairman
John M. W. Moorlach**
Second District

Buena Park (portions of), Costa Mesa, Cypress, Fountain Valley (portions of), Huntington Beach, La Palma, Los Alamitos, Newport Beach, Seal Beach, Stanton



**Chairman
Bill Campbell**
Third District

Anaheim (portions of), Irvine (portions of), Orange, Tustin, Villa Park, Yorba Linda



**Supervisor
Shawn Nelson**
Fourth District

Anaheim (portions of), Brea, Buena Park (portions of), Fullerton, La Habra, Placentia



**Supervisor
Patricia C. Bates**
Fifth District

Aliso Viejo, Dana Point, Irvine (portions of), Laguna Beach, Laguna Hills, Laguna Niguel, Laguna Woods, Lake Forest, Mission Viejo, Rancho Santa Margarita, San Clemente, San Juan Capistrano



GOVERNANCE & ACCOUNTABILITY

(COMPLETED 37 REPORTS TO BOS AND AOC)

REPORTING STRUCTURE

BOARD OF SUPERVISORS

IAD's Independence Complies with Best Practices

The Director of Internal Audit reports directly to the Board of Supervisors, which is the highest governing body of the County. This reporting structure is the most prevalent one for the largest counties and cities in the U.S. and the one that fully complies with independence standards required by the AICPA, IIA, and Government Accountability Office (GAO). The Board of Supervisors share in the elected responsibility and accountability for financial stewardship of the entire County.

We strive to meet the Board's expectations for integrity, objectivity, and independence, and to function effectively with consistent reliability and credibility. The IAD applies professional auditing standards to all engagements. This allows us to ensure reviews and assessments of County operations are always informative, accurate, and objective.

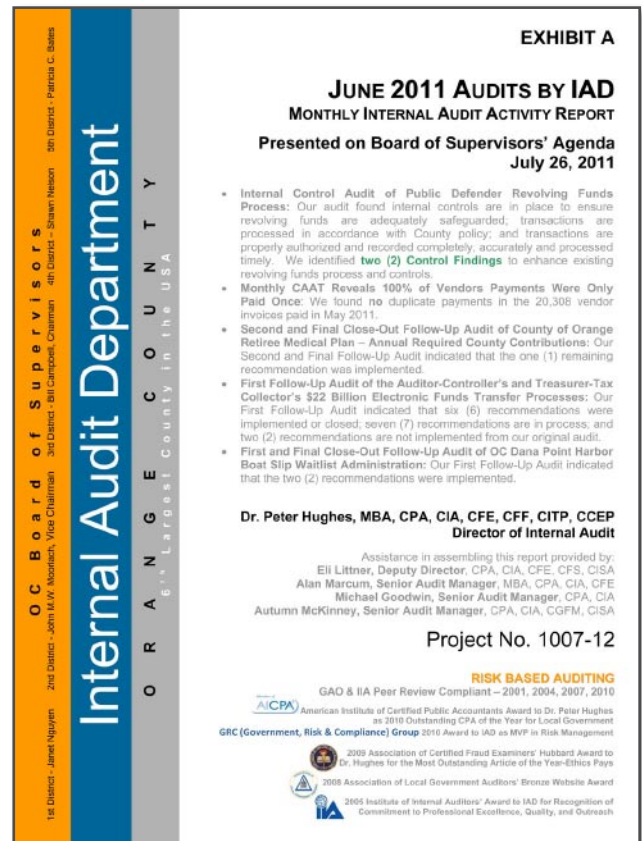
OC INTERNAL AUDITOR'S ANNUAL REPORT FOR FY 2009-10.

Each year the IAD prepares an annual report to the Board of Supervisors that provides highlights and accomplishments of the audit activities during the prior fiscal year.

IAD'S MONTHLY INTERNAL AUDIT ACTIVITY REPORT TO THE BOARD OF SUPERVISORS.

As a direct report to the Board, the Director of Internal Audit submits to the Board (in public forum) a monthly summary of all audit reports issued for the prior month. We prepared **12** Monthly Internal Audit Activity Reports for FY 10/11.

This formal communication to the Board allows for more detailed discussions of audit reports and issues in the public setting. The heightened level of exposure ensures the transparency of the audit process. This report identifies all audits and follow-up audits completed for the month, and includes detailed descriptions of the scope, conclusions, background, and type of recommendations. In addition, the Monthly Internal Audit Activity Report provides a summary of completed audits and follow-ups and a description of any significant risks, control or governance issues, and a listing by severity of audit findings identified in the audits.



Monthly Internal Audit Activity Report

Government

Elected Officials, Citizenship and Voting





FY 2010/2011 INTERNAL AUDITOR'S ANNUAL REPORT



GOVERNANCE & ACCOUNTABILITY (CONTINUED)

AUDIT OVERSIGHT COMMITTEE REPORTS

AOC Adheres to Best Practice

The Board of Supervisors (BOS) also created the Audit Oversight Committee (AOC) as an advisory group to provide quarterly oversight of the progress of the Internal Audit Department in completing its Annual Audit Plan. The AOC membership, set by the Board of Supervisors, includes the Chairman and Vice-Chairman of the Board, Auditor-Controller, Treasurer-Tax Collector (ex-officio member), County Executive Officer, Performance Audit Director (ex-officio member), and 3 public members. As specified in Board Resolution 95-271 entitled "Establishment of an Internal Audit Unit Independent from the County Auditor-Controller Reporting Directly to the Board of Supervisors," the Board directed the "CEO and Auditor-Controller to effect the transfer of internal audit responsibilities and staff from the Auditor-Controller's Office to the Internal Audit Unit" and clarified that "the Oversight Committee will not have direct control over the Internal Audit Unit. Direct control will be exercised by the Board of Supervisors."

For the FY 10/11 quarterly AOC meetings, we prepared a total of **24** reports as follows:


- Four (4) *Quarterly Status Reports* listing all audits, follow-ups, and control related & other assignments, along with the budget, actual hours charged, variance between budget and actual, and milestone comments.
- Four (4) *External Audit Coverage Reports* identifying external audits being conducted in the County, as reported to us by the Departments/Agencies, and an executive summary which identifies the total audits in progress, planned, and/or completed, along with any critical/material issues identified.
- Twelve (12) *Executive Summaries of Audit Assignments* providing a summary of findings for audits and follow-up audits.
- Four (4) *IT Briefing Reports* summarizing the work performed in the area of IT audits and Internal Audit's involvement with system implementations, such as CAPS+ and PTMS.

The *Quarterly Status Report* in combination with the *IAD Monthly Internal Audit Activity Report* and the *Internal Auditor's Annual Report* fulfill the Audit Director's obligation to report to the Board of Supervisors, the OC Internal Audit Department's purpose, authority, and performance relative to its annual audit plan as prescribed by the Institute of Internal Auditors (IIA) Professional Standard 2060.

IAD'S COUNTY RISK MANAGEMENT ROLE (COMPLIES WITH IIA PROFESSIONAL STANDARD 2020 - RISK MANAGEMENT)

Risk management is a key responsibility of senior management and the Board of Supervisors. The OC Internal Audit Department's role directed by the Board approved Charter and Administrative Rules is to provide support to the Board of Supervisors and Countywide "risk management processes" in the following four ways:

1. Participating and providing risk/control insights to various County oversight committees such as the CAPS+ Steering Committee, PTMS Steering Committee, Business Continuity Working Group, Financial Managers Forum, Human Resources Leadership Forum, Purchasing Council, HIPAA Coordinator Group, Property/Surplus Equipment Officer Group, RFP committees for large contracts, and Department Head meetings.

A G E N D A	
REGULAR MEETING OF THE AUDIT OVERSIGHT COMMITTEE ORANGE COUNTY, CALIFORNIA	
WEDNESDAY, April 27, 2011, 10:00 a.m.	
HALL OF ADMINISTRATION 333 Santa Ana Blvd., 5th Floor Conference Room A Santa Ana, California	
	
Supervisor Bill Campbell Member	Supervisor John M.W. Moorlach Member
Thomas G. Mauk Chairman	David E. Sundstrom Vice-Chairman
Dr. David Carlson Public Member	Shari L. Freidenrich Ex-Officio Member (non-voting)
Steve Danley Ex-Officio Member (non-voting)	
Director of Internal Audit County Counsel Clerk	Dr. Peter Hughes, CPA Ann Fletcher Renee Aragon
<small>The Audit Oversight Committee (AOC) welcomes you to this meeting. This agenda contains a brief general description of each item to be considered. The AOC encourages your participation. If you wish to speak on an item contained in the agenda, please complete a Speaker Form identifying the item(s) and deposit it in the Speaker Form Return box located next to the Clerk. If you wish to speak on a matter which does not appear on the agenda, you may do so during the Public Comment period at the beginning of the meeting. Except as otherwise provided by law, no action shall be taken on any item not appearing in the agenda. When addressing the AOC, please state your name for the record prior to providing your comments.</small>	
<small>**In compliance with the Americans with Disabilities Act, those requiring accommodation for this meeting should notify the Internal Audit Department 72 hours prior to the meeting at (714) 834-5475**</small>	
<small>All supporting documentation is available for public review in the office of the OC Internal Audit Department located in the Hall of Finance and Records Building, 12 Civic Center Plaza, Room 232, Santa Ana, California 92701 during regular business hours, 8:00 a.m. - 5:00 p.m., Monday through Friday.</small>	
10:00 A.M.	
1. Roll Call	
2. Approve Audit Oversight Committee regular meeting minutes of February 23, 2011	
3. Receive Single Audit Report and related letters for fiscal year ending June 30, 2010 from external auditors Vavrinek, Trine, Day and Company, LLP	
4. Approve Fiscal Year 2011-2012 Audit Plan and Risk Assessment	
AGENDA - AUDIT OVERSIGHT COMMITTEE MEETING, WEDNESDAY, APRIL 27, 2011 - PAGE 1	

AUDIT OVERSIGHT COMMITTEE REPORT AGENDA



GOVERNANCE & ACCOUNTABILITY (CONTINUED)

2. Compiling, assessing, and providing written quarterly status reports of all External Audits performed throughout the County (such as those conducted by State and Federal Auditors) to the Board of Supervisors and Audit Oversight Committee (AOC). These quarterly reports highlight material issues and significant findings identified by external auditors, providing visibility to various financial, compliance, programmatic, and regulatory issues and risks. The AOC Administrative Procedure No. 2 (approved by the Board of Supervisors) established the OC Internal Audit Department's responsibility for this report.
3. Performing and distributing OC Internal Audit Department's Annual Risk Assessment to the BOS, AOC, and Department Heads, as well as posting on our website, gives visibility of the risk ratings we assign to the County's key business processes and systems. To help determine the risk ratings, among other things we send out departmental risk assessment surveys, conduct interviews with key executive management, and review departmental business plans to determine business strategies and risks. See further details about our Annual Risk Assessment on page 14.
4. Distributing all internal audit reports to the Board of Supervisors, AOC, and Department Heads, as well as posting on Internal Audit's website, to give Countywide visibility to findings and related risks identified.

QUALITY ASSURANCE & IMPROVEMENT PROGRAM

IAD Receives Highest Possible Rating

Who Audits the Internal Auditors? California Government Code and the audit profession require that auditors be audited at least every three years. This audit is called a **Peer Review or Quality Assessment**. A Peer Review assesses an **audit department's adherence to over 150 professional standards and practice advisories**.

The Institute of Internal Auditors (IIA) Professional Standard 1300 requires that the Chief Audit Executive (CAE) develop and maintain a Quality Assurance and Improvement Program (QAIP) that covers all aspects of the internal audit activity. The QAIP must include both internal and external assessments.

Internal Assessments (IIA Professional Standard 1311), Internal assessments must include:

- I. Ongoing Monitoring of the Performance of the Internal Audit Activity The OC Internal Audit Department performs the following:
 1. Ongoing supervision of all audits through timely review of audit work papers and reports.
 2. Uses Quality Assurance checklists on every audit.
 3. Surveys all of its "auditees" with a Customer Survey of Audit Services to obtain the client's perspective of the audit process. The Customer Survey consists of nine questions pertaining to the value and competency of the audit and auditors. At year end, we tabulate the customer survey results to measure performance and help identify where improvements can be made.
 4. Senior Audit Managers perform annual internal assessments of each others' audits and provide feedback on the results of the assessments.
 5. Uses project budgets, timekeeping, audit plan tracking, and identification of cost recoveries.
 6. All levels of management perform formal, structured reviews and approval of all official releases by the Director of Internal Audit.
- II. Periodic Internal Reviews Performed Through Self-Assessment The OC Internal Audit Department performs the following:
 1. Periodic in-depth interviews of key department heads and administrators.
 2. Periodic "self-assessments" including all of its staff, auditors, and managers using an anonymous survey addressing the department's compliance with professional auditing standards and charter.



FY 2010/2011 INTERNAL AUDITOR'S ANNUAL REPORT

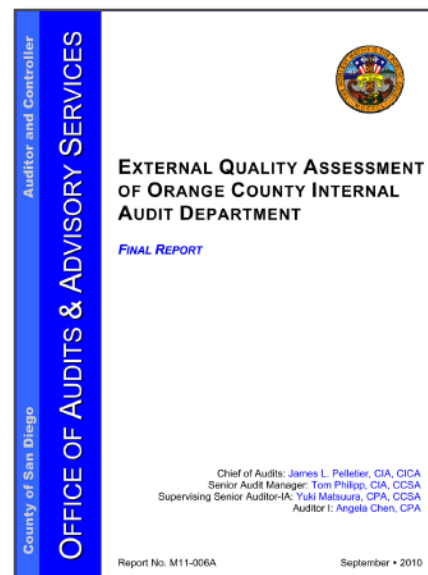


3. Reviews the Association of Local Government Auditors Biennial Benchmarking and Best Practices Survey as a comparison for performance metrics.
4. Reports annually a "Balanced Scorecard," the results of meeting its performance objectives now included in the business plan process.


We are happy to report that our internal assessment for FY 10/11 confirmed we continue to comply with professional auditing standards and have incorporated many of the best practices of the profession.

External Assessments (IIA Professional Standard 1312) Peer Reviews/Quality Assessments are conducted on the OC Internal Audit Department every three years. In June 2010, the County of San Diego's Office of Audits & Advisory Services conducted our most recent Peer Review and found that we conformed to the IIA Standards and Code of Ethics with the highest possible rating. In the last 10 years, the OC Internal Audit Department has had four Peer Reviews and each time received the best ratings possible.

IIA Professional Standards also require that the chief audit executive communicate the results of the Peer Review/Quality Assessment to the Board of Supervisors. The results are communicated in Audit Oversight Committee meetings, within our annual Business Plan, by individual meetings between the Director of Internal Audit and Board of Supervisors' members, and in our Annual Internal Auditor's Report.



EXTERNAL QUALITY ASSESSMENT (PEER REVIEW)



NEWS

ORANGE COUNTY GRAND JURY

Date March 25, 2008 700 CIVIC CENTER DRIVE WEST • SANTA ANA, CALIFORNIA 92701 • 714/834-3320
FAX 714/834-5555

BANKRUPTCY CONTROLS – GOING, GOING ...

SANTA ANA, CALIFORNIA - The 2007-2008 Orange County Grand Jury recently released a report regarding Orange County's bankruptcy controls.

The Board of Supervisors recently considered a proposal to return the Internal Audit Department to the Auditor-Controller's office – the same reporting structure held partially responsible for the County's 1994 bankruptcy. The 2007-2008 Grand Jury has concluded that the Orange County's Internal Audit Department (IAD) has the formal independence and procedures to meet both public and private internal audit standards.

The Grand Jury recommends that the Internal Audit Department remain independent and continue to report directly to the Board of Supervisors. The Grand Jury found that the current organizational reporting structure provides maximum auditor independence and reinforces Board accountability for the financial security of the County.


As a result of the bankruptcy, the Board in 1995 took steps to shield the Internal Audit Department from any potential management influence. Organizational independence of the Internal Auditor was established by having the IAD report directly to the Board and not to the Auditor-Controller.

Professional and governmental auditing standards require that internal audit organizations be free from personal, external and organizational impairments to independence in auditing matters. The office of County Counsel has concluded that the Internal Audit Department does not report to any department or office it audits. As such the IAD appears to satisfy the GAO (Government Accountability Office) standards relating to organizational independence.

The Grand Jury also recommends that the Board of Supervisors add additional members to the Audit Oversight Committee representing primary stakeholders in the County Treasury, such as one appointed by the Orange County Board of Education to represent school districts and one appointed by the Orange County League of Cities to represent cities.

The failure of the audit function in 1994 contributed to a disaster which cost the taxpayers of Orange County hundreds of millions of dollars. This tragedy may not have occurred had there been and independent system of organizational checks and balances over Treasury operations. The structure of Orange County government, prior to the Chapter 9 filing in December 1994, failed to provide the warning signs necessary to protect the County's solvency. We ignore the lessons learned from the bankruptcy at our own peril. The recent push to re-establish the audit structure existing prior to 1994 is unnecessary, untimely and unwise. The Internal Audit Department serves Orange County well and should not be tampered with.

For a full version of this report, as well as others, visit the Grand Jury website at www.ocgrandjury.org or call (714) 834-3320.

2007-2008 ORANGE COUNTY GRAND JURY

Ann Ayres Andress, Foreman

Become a part of the Grand Jury process, call (714) 834-6747 for information and an application.

GRAND JURY REPORT

OCIAD Should Continue Reporting Directly to Board

On March 25, 2008, the 2007-2008 Orange County Grand Jury in their report titled "*Bankruptcy Controls – Going, Going, ...*" concluded that the Internal Audit Department should remain independent and continue to report directly to the Board of Supervisors, and that the current organizational reporting structure provides maximum auditor independence and reinforces the Board of Supervisors' accountability for the financial security of the County.

Each county is required by law to impanel a Grand Jury to serve for a term of one year and is mandated to investigate and report on civil and criminal matters within the county. The civil or "watchdog" responsibilities of the Grand Jury include the examination of all aspects of County government, including special districts, to ensure the County is being governed honestly and efficiently and County monies are being handled appropriately.

The Orange County Grand Jury meets with the OC Internal Audit Department each year as a new Grand Jury is assembled. They meet with the Director and gain an understanding of the audit services we provide and how the Annual Risk Assessment and Audit Plan are developed. On occasion, members of the Grand Jury will attend the quarterly Audit Oversight Committee meetings to observe the oversight meetings in public forum.



■ INTERNAL AUDIT NOTEWORTHY NEWS

IN 2011:

- **Peter Hughes elected as AICPA Ambassador for 3 year term** for their Government Performance and Accountability Committee (GPAC). In this capacity Dr. Hughes along with fellow "Ambassadors" represent GPAC to a world-wide audience. Dr. Hughes' expertise in developing controls to identify and stop fraud will be on display in February 2012 as a Key Note Speaker at a "Thought Leadership" Symposium in Australia. In addition, he provided a free one-day workshop in October 2011 on detecting and stopping fraud for the California State Association of Counties (CSAC).
- **Computer Assisted Auditing Techniques (CAATs)**
The OC Internal Audit Department's IT Auditors developed and presented a training course for the Information Systems Audit and Control Association (ISACA) LA Spring 2011 Conference about our use of CAATs in developing the Annual Audit Plan and Risk Assessment and in conducting audits. CAATs give auditors the ability to audit 100% of transactions rather than on a sample basis. In addition, we wrote an article about the CAAT routines and their use within Orange County. The article was published in the Association of Local Government Auditor's (ALGA) Quarterly Journal for Summer 2011.
- **Internship in Internal Audit**
This year the OC Internal Audit Department implemented an internship program to provide support, under close supervision, in performing a variety of routine internal auditing work of the department, such as financial audits and mandates and internal control audits. Mr. Michael Steinhaus, our Internal Auditor Intern, will obtain audit experience, training, and mentoring in the profession of internal auditing. Mr. Steinhaus is a recent graduate of California State University, Fullerton and successfully and impressively completed all four parts of the CPA exam at his first attempt. He is currently working towards obtaining his professional CPA license.

IN 2010 – AICPA

The American Institute of Certified Public Accountants (AICPA) named Dr. Peter Hughes as **2010 CPA of the Year for Local Government**. Only one out of 360,000 of total CPAs is selected for this recognition. This award is based upon rigorous criteria that ensure the recipient meets the highest professional standards.



IN 2009 – ACFE

The Association of Certified Fraud Examiners (ACFE) recognized the contributions of anti-fraud professionals worldwide with the prestigious ACFE Outstanding Achievement Award – 2009 Hubbard Award to Dr. Peter Hughes, CFE, CPA for the most popular article of the year, entitled *Ethics Pays in So Many Ways*.



IN 2008 – ALGA

The Internal Audit department was awarded the Association of Local Government Auditors (ALGA) Bronze Website Award for its informational and user-friendly audit website (www.ocgov.com/audit). ALGA is a national organization dedicated to promoting and advancing the audit profession.



IN 2005 – IIA

The Internal Audit Department received the highly prestigious "Recognition of Commitment" to professional excellence, quality and outreach from the Institute of Internal Auditors (IIA).





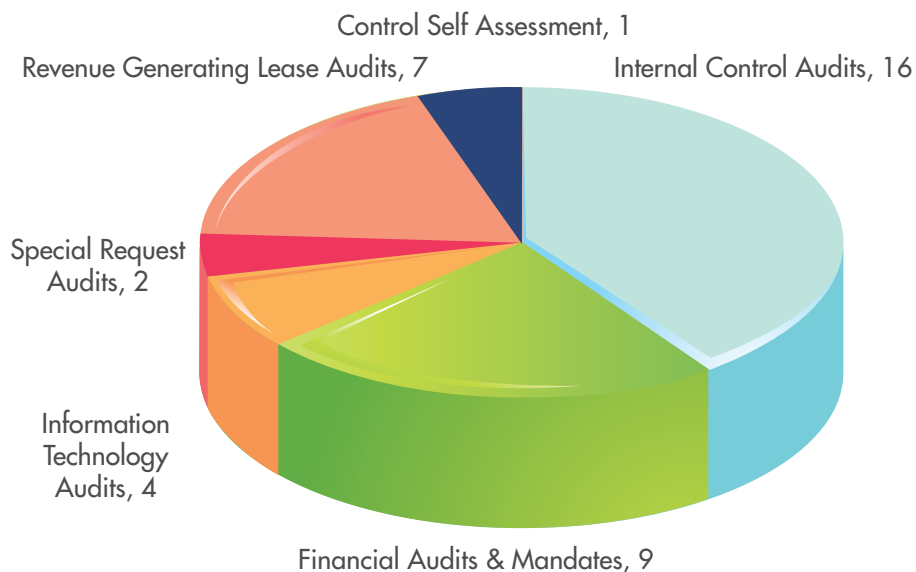
FY 2010/2011 INTERNAL AUDITOR'S ANNUAL REPORT



FY 2010/2011 DETAILED ACCOMPLISHMENTS

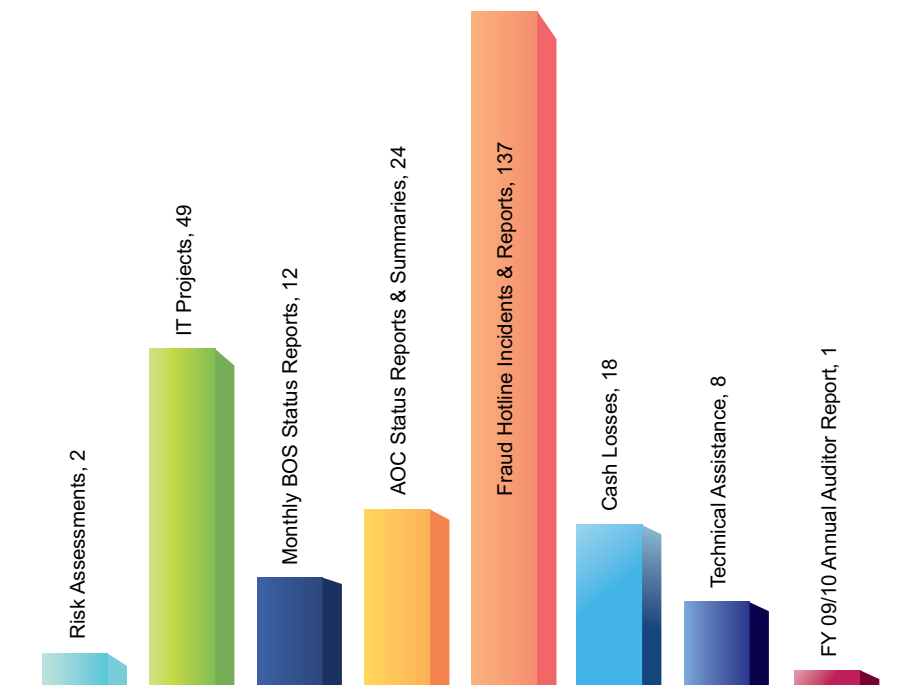
39 AUDITS COMPLETED

Our "Audits Completed" count represents the completed audits in the FY 2010/11 Audit Plan, which was developed based upon our annual Risk Assessment and approved by the Audit Oversight Committee and Board of Supervisors.



251 AUDIT PROJECTS COMPLETED

Our "Audit Projects Completed" represent various reports and projects generated for purposes of planning and risk assessment; fraud hotline management; performing computerized auditing routines; monitoring cash losses; and preparing reports to the Board of Supervisors and Audit Oversight Committee for governance and accountability over the Internal Audit function.





■ INTERNAL CONTROL AUDITS

We completed 10 Audits and 6 Follow-Up Audits. Internal Control Audits (ICAs) determine the adequacy and integrity of controls in critical business processes by providing reasonable assurance over the recording, reporting, and reconciling of financial transactions, safeguarding County assets, compliance with department and County policies, and evidence of process efficiencies and effectiveness. We performed the following ICAs during FY 10/11:

1. Health Care Agency Fee Generated Revenue. We audited the adequacy of internal controls over fee studies and fee development processes for establishing cost-recovery fees charged to the public. HCA had **fourteen fee studies** that required Board approval and received **fee generated revenue totaling \$18 million.**

2. OC Waste & Recycling Fee Generated Revenue. We audited the adequacy of internal controls over fee development processes for establishing cost-recovery fees charged to the public. OC Waste & Recycling generated **\$93 million in fee revenue.**

3. Health Care Agency Disbursement Approval Process. We audited the adequacy of internal controls for approving and processing disbursements (payments to vendors for commodities and services). HCA disbursed over **\$659 million in expenditures.**

4. OC Waste & Recycling Disbursement Approval Process. We audited the internal controls used for approving and processing disbursements (payments to vendors for commodities and services). OC Waste & Recycling **disbursed over \$54 million in expenditures** for commodities and services.

5. OC Public Works Countywide Fleet Management. We audited OC Fleet Services to evaluate their oversight role for Countywide fleet management, including the administration of fleet assignment and enforcement of vehicle rules and regulations. OC Fleet Services' **inventory consisted of 2,477 vehicles** assigned to agencies/departments and **42 pool vehicles** available to County employees.

6. OC Public Works County Fuel Card Administration. We audited OC Fleet Services to evaluate their administration of County Fuel Access Cards and Voyager Fleet Cards provided to employees for fueling of assigned County vehicles. **\$3.8 million** was spent by departments/agencies using County Fuel

Access Cards and Voyager Fleet Cards. There were approximately **4,700 active Fuel Access Cards and 1,000 active Voyager Fleet Cards.**

7. Health Care Agency Contract Development and Management Payment Approval and Fiscal Monitoring. We audited the adequacy of internal controls over Contract Development and Management's (CDM) payment approval and fiscal monitoring processes. CDM administered **496 contracts totaling \$271 million**, and processed **\$198 million in contractor invoices.**

8. OC Dana Point Harbor Boat Slip Waitlist Administration. We audited the administration of boat slip waitlists at OC Dana Point Harbor to ensure boat slips are assigned properly, orderly and fairly. There are **2,915 boat slips** and dry boat storage spaces available to the public. There were **29 waitlists with 3,378 applicants.**

9. Public Defender Revolving Funds. We audited internal controls to ensure revolving funds are adequately safeguarded; transactions are processed in accordance with County policy; and transactions are properly authorized, recorded completely, accurately and processed timely. The Public Defender incurred **\$1.5 million in revolving fund expenditures.**

10. County Counsel Revolving Funds. We audited internal controls to ensure revolving funds are adequately safeguarded; transactions are processed in accordance with County policy; and transactions are properly authorized, recorded completely, accurately and processed timely. County Counsel incurred **\$33,000 in revolving fund expenditures.**

11. Follow-Up Audits. 6 Follow-Up Audits were completed (2 integrated follow-up audits are also counted under the IT audits). Follow-Up Audits are necessary to ensure that audit recommendations are implemented satisfactorily. We perform our First Follow-Up Audit six



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months from the date of the original audit report. If any items are not fully implemented, a Second Follow-Up Audit is conducted 12 months from the date of the original audit report. We conducted the following Follow-Up Audits: **County Fee Development Monitoring Process; Electronic Fund Transfers; CEO/Risk Management Disbursements; OC Dana Point Harbor Boat Slip Waitlist Administration; Probation Title IV-E Claims; and OC Public Works/OC Fleet Services Interdepartmental Billing.**

■ FINANCIAL AUDITS & MANDATES

We completed 6 Audits and 3 Follow-Up Audits.

- 1. District Attorney Workers' Compensation Fraud Grant Audit**
- 2. District Attorney Health & Disability Insurance Fraud Grant Audit**
- 3. District Attorney Insurance Fund Fraud Grant Audit**
- 4. District Attorney Auto Fraud Activity Interdiction Grant Audit**

In the District Attorney grant audits, we determine that the financial statements are fairly stated in accordance with applicable professional standards, financial statements are supported by sound internal controls, and that management complied with applicable laws, regulations, and grant requirements. These audits are conducted in accordance with generally accepted auditing standards of the United States of America, and/or Government Auditing Standards issued by the Comptroller General of the United States.

5. Treasurer-Tax Collector Annual Compliance Audit (12/31/09)

In the Treasurer-Tax Collector Annual Compliance Audit we determined the Orange County Treasurer's compliance with the California Government Code (sections 27130 - 27137) and related provisions of the Orange County Investment Policy Statement. This audit is mandated by California Government Code and is conducted in accordance with generally accepted auditing standards of the United States of America.

6. Treasurer-Tax Collector Audit of Treasury Cost Allocation to Pool Participants

In the Audit of Treasury Cost Allocations to Pool Participants, we (1) evaluated internal controls for the calculation and allocation of administrative costs to investment pool participants; (2) determined if administrative costs allocated to investment pool participants were properly authorized and processed completely, accurately, timely, and in accordance with relevant California Government Codes, and department policies and procedures; and (3) determined if the allocation processes were efficient and effective. This audit was conducted in conformance with the Institute of Internal Auditors' International Standards for the Professional Practice of Internal Auditing.

We completed 3 follow-up Financial and Mandated Audits listed in the FY 10/11 Audit Plan on schedule as follows:

- 7. Follow-Up Audit of CAFR Financial Statement Footnote Disclosures**
- 8. First Follow-Up Audit of Retiree Medical Annual Required Contribution**
- 9. Second Follow-Up Audit of Retiree Medical Annual Required Contribution**



■ INFORMATION TECHNOLOGY (IT) AUDITS

We completed **4** follow-up audits, and **49** projects in this category as listed below. In these audits, we review controls in a variety of information technology areas including general controls, application controls, and system developments. We performed work in the following IT areas during FY 10/11:

1. New System Implementation Assistance: We worked on **3** projects as described below. We consider our work on each project to be "completed" for this fiscal year, even if our assistance will continue in the following fiscal year:

Overview: We provide internal control assistance to selected key financial system implementations. Our role is limited to reviewing and providing feedback on the internal controls contained in written procedures, process flowcharts, and other process and control documentation prepared for the new system by the implementation team. The primary purpose of our review is to review and provide feedback whether selected processes being developed and related documentation contain appropriate internal controls in the four key areas of:

- ▶ Proper segregation of duties;
- ▶ Appropriate reviews and approvals;
- ▶ Audit trails related to preservation of source documents and recording of reviews and approvals; and
- ▶ Sound account reconciliations.

We also attend selected project and governance meetings. Depending on the nature of our feedback, it can be verbal, in an email or in a written report known as an "Audit Alert" to provide "just in time" input to the implementation. During FY 10/11, we provided assistance to the following 3 system implementation projects:

■ **CAPS+ Human Resources/Payroll System Implementation (Audit No. 1046):** The CAPS+ system was successfully implemented in February 2011 by the CAPS+ Implementation Project Team. Our internal controls assistance is completed on this implementation project. We will continue to attend future monthly CAPS+ Steering Committee meetings.

■ **Property Tax Management System (PTMS) Implementation (Audit No. 1047)**

▶ **Tier 2 and Tier 3 Modules:**

We attended oversight meetings and reviewed documentation for a sample of the Tier 3 key business processes. We reviewed a majority of the draft high-level design documentation created by the PTMS Project Team for payment processing, penalty cancellations, and tax refunds (Tier 3 Modules). As the high-level design documentation is completed for each module, the PTMS Project Team moves on to create the low-level design documentation. These PTMS modules are scheduled to go-live in July 2012. Our assistance will continue in FY 11/12 for this implementation.

■ **OC Public Administrator Conservatorship System (OCPACS) Implementation (Audit No. 2952):** We reviewed selected documentation available for the case management, accounting, and asset management modules. As of June 30, 2011, we have been awaiting additional documentation (such as updated systems role matrix to evaluate segregation of duties and user access/authentication procedures) from the OCPACS Project Team. According to the OCPACS Project Team, there have been vendor delays and the OCPACS Project Team has been focusing their efforts on remediation. Update: we were subsequently informed that as of October 2011 the project is canceled due to the vendor's inability to complete outstanding deliverables.

2. Computer Assisted Audit Techniques (CAATs): We use a proprietary, state-of-the-art/best practice software product to help us analyze data for payroll and vendor payments. The audit work is commonly known as Computer Assisted Audit Techniques (CAATs). We completed **46** projects in this category:

■ **Duplicate Vendor Payments:** We conducted **12** monthly CAAT routines to identify potential duplicate vendor payments. Since the inception of this routine in May 2002, duplicate payments identified are \$979,804 and amounts recovered are \$941,848, for a recovery rate of approximately 96%.

■ **Working Retirees/Extra-Help Hours:** We performed **12** monthly reviews of working retiree activity reports to identify retirees who exceed hourly limits and noted no working retirees exceeded annual limits for FY 10/11.



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■ **Employee/Vendor Address Match:** We performed **4** CAAT routines to identify employees that share a similar address with a vendor, which could be an indicator of employees buying goods or issuing contracts to themselves or a related vendor. We identified one (1) potential employee-vendor match that was provided to the Human Resources Department (HRD) for further review. HRD determined no conflict existed for the potential employee-vendor match.

■ **Direct Deposits:** We performed **12** CAAT routines to identify multiple employee paychecks directly deposited to the same bank account, which could be an indicator of inappropriate payments. We noted no findings.

■ **Annual Risk Assessment:** We performed several CAAT routines (count as **1** project) to obtain financial information (transaction amounts and activity) utilized in the annual risk assessment. For example, we re-sort and compile cash receipt activity by the department processing the cash receipt rather than by the department/fund where the money is deposited.

■ **Rewrite CAAT Routines:** The new CAPS+ Financial system changed the reports and data fields for some of our CAAT routines. We completed and implemented new annual risk assessment routines using CAPS+ year-end reports as of 6/30/10 (count as **1** project).

■ **New CAAT Routine:** We developed new fuel card CAAT routines (count as **1** project). We wrote one-time CAAT routines to analyze fuel card activity to assist the Internal Control Audit of County Fuel Card Administration (Audit. No. 1029). The analysis included comparison of fuel card data with human resource data.

■ **Audit Alert (No. 1041-E):** During our quarterly CAAT reviewing for possible employee-vendor conflicts of interest, we identified an issue related to a former employee working as both an extra help retiree and contractor within the same year (no overlapping dates). In the Audit Alert, we identified and communicated opportunities for the CEO to clarify working relationships with former employees and to reduce policy confusion (count as **1** project).

■ **CAAT Training Course:** We developed and presented a training course about OCIAD's use of CAATs for the ISACA LA Spring 2011 Conference (count as **1** project).

■ **Published CAAT Article:** We wrote an article about OCIAD's CAAT routines and use within Orange County.

The article was published in the Association of Local Government Auditor's (ALGA) Quarterly Journal for Summer 2011 (count as **1** project).

3. Follow-Up Audit: We completed **4** follow-up audits as listed below:

■ **First Follow-Up Audits - Treasurer-Tax Collector's Controls Over Compliance with PCI DSS (Audit No. 1050-A):** Our First Follow-Up Audit found that the Treasurer-Tax Collector, Auditor-Controller, OC Public Works, CEO/Procurement, and OC Community Resources fully implemented nine (9) recommendations and three (3) recommendations are in process from our original audit.

■ **First Follow-Up Audit - CAPS+ Financial System Oracle Database Configuration (Audit No. 1050-B):** Our First Follow-Up Audit found that the CAPS Steering Committee (supported by the Auditor-Controller and CEO/IT) fully implemented nine (9) recommendations and one (1) recommendation is in process from our original audit.

■ **First Follow-Up Audit - Auditor-Controller's and Treasurer-Tax Collector's \$22 Billion Electronic Funds Transfer Processes (Audit No. 1033-C):** Our First Follow-Up Audit found that the Auditor-Controller, Treasurer-Tax Collector, and CEO/IT fully implemented or closed six (6) recommendations, seven (7) recommendations are in process, and two (2) recommendations have not been implemented. The follow-up was an integrated audit.

■ **First Follow-Up Audit - OCPW Transportation Interdepartmental Billing Process (2927-D):** Our First Follow-Up Audit found that OC Public Works Transportation/Fleet Services fully implemented eleven (11) recommendations, partially implemented one (1) recommendation, and one (1) recommendation is in process from our original audit. The follow-up was an integrated audit.

BEST PRACTICE BY OC IAD

OC IAD is one of the few counties to have developed an ongoing CAAT program.



COUNTYWIDE RISK ASSESSMENT

We completed 2 Risk Assessments. The OC Internal Audit Department conducts a comprehensive, interactive countywide Risk Assessment for purposes of establishing the annual Audit Plan. The Risk Assessment consists of a **general risk assessment** for critical business processes common throughout the County (e.g. cash receipts and disbursements, accounts receivables and payables, purchasing and contract administration, payroll, budgets, etc.) and an **information technology inventory and assessment** where key systems are identified and rated as to levels of risk. The Risk Assessment includes reviews of Business Plans; meetings with the Board of Supervisors and the County Executive Office; and meetings and/or correspondence with all departments/agencies to obtain their input on risks affecting their respective areas.



For FY 10/11, we completed risk assessments for 22 departments/agencies (excluding Internal Audit, the Office of Independent Review, and the Office of the Performance Auditor), five Board Offices, and one comprehensive Risk Assessment for Information Technology that consolidated information from all County departments/agencies.

AUDIT ALERTS - PROMPT REPORTING FOR IMMEDIATE ACTION

In response to the Board of Supervisors' request to bring to their attention audit issues on urgent matters, we began issuing Audit Alerts in 2007 and continue to use this method of reporting aimed at **elevating the issues** to the Board and Management for **immediate** attention and action.

The Audit Alert was designed to identify and highlight significant audit issues impacting the County. Our focus was not just informing the Board, but to aid County management with proper stewardship to identify risk and provide timely recommendations for resolutions. In due diligence, the Audit Alert was developed and applied as a "Best Practice."

In 2007/2008 we issued seven Audit Alerts; in 2008/2009 we issued three Audit Alerts; and in 2009/10 we issued two Audit Alerts. **We issued one Audit Alert in FY 10/11.** As such, a total of **13** Audit Alerts have been issued since 2007. Audit Alerts are presented to the Board through the *Monthly Internal Audit Activity Report*.

SPECIAL REQUEST AUDITS

2 Audits Completed. During FY 2010-2011, OC Internal Audit performed the following compliance/special request audits from the Board of Supervisors and/or Audit Oversight Committee:

1. Treasurer-Tax Collector – Tax Collections and Cash Receipts At the direction of the Board of Supervisors, we audited the Treasurer-Tax Collector Tax Collection and Cash Receipt processes and the controls regarding tax refunds and the cancellation of penalties charged for late payments on property taxes. The Treasurer-Tax Collector **processed \$5.3 billion in tax collections and cash receipts** during the audit period.

2. Community Facility Districts (CFDs) – Ladera Ranch At the direction of the Audit Oversight Committee, we audited the six (6) Ladera Ranch Community Facility Districts to determine if the special tax rates are calculated in accordance with pertinent governing documentation, and if bond proceeds used for projects are in compliance with pertinent governing documentation. The six CFDs for Ladera Ranch received principal **bond proceeds totaling \$287 million.** As a result of our audit, **the Special District/Mello-Roos taxes for all 23 CFDs** (6 in Ladera Ranch and 17 others) **were lowered nearly \$20 million over the next three years.**



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■ CONTROL SELF-ASSESSMENT & PROCESS IMPROVEMENT

Control Self-Assessment & Process Improvement (CSA-PI) is a process by which the managers and employees of a unit and trained facilitators from Internal Audit have a workshop to discuss the strengths and concerns which impact their ability (individually and as a group) to meet their objectives. CSA-PI is not an audit; rather, it is an audit technique within the broad framework of internal audit that measures areas that traditional audit techniques are not designed to measure, such as trust, morale and corporate culture. **Over the past 10 years, Internal Audit has conducted over 100 workshops.**

In FY 10/11, we facilitated **two CSA-PI workshops** in the **Treasurer-Tax Collector** at the request of the newly-elected Treasurer-Tax Collector because of several changes in executive management over the past five years. After completion of the two CSA-PI workshops, each team worked with management to prepare an internal **Action Plan** which addressed the higher-priority issues brought forward during the workshops.

■ TECHNICAL ASSISTANCE TO DEPARTMENTS/AGENCIES

8 Projects Completed The OC Internal Audit Department provides technical assistance to County departments/agencies upon request by department/agency Directors. While not considered an audit, technical assistance can include participating on Request for Proposal (RFP) evaluation panels as job knowledge experts, performing a cursory, high-level review of various technical issues, or providing limited technical consultation services. During FY 2010/2011, OC Internal Audit Department provided the following technical assistance to departments/agencies:

- 1. OCCR – Review of Eli Home Inc.** – At the request of the OCCR Director, we performed a limited review of the Eli Home Inc. Form 990 for Tax Year 2008, and the independently Audited Financial Statements Single Audit Report on Federal Awards for the Year Ended December 31, 2009.
- 2. OCCR – Review of Age Well Senior Services** – At the request of the OCCR Director, we performed a limited review of the Age Well Senior Services Form 990s for Tax Years 2008 and 2009, and the Audited Financial Statements for the Years Ended June 30, 2010, and 2009. We also conducted a preliminary assessment of the organization's internal controls through a site visit, interviews, and examination of related documents.
- 3. CEO/IT - IT Sourcing RFP** – We participated on the IT Sourcing RFP by providing advice and insights on effective pricing strategies for this costly complex RFP. This RFP is a multi-year, large dollar outsourcing contract for the enterprise data center and telephone services (including converging the old telephone system with new VOIP technologies). This assistance will continue in FY 11/12.
- 4. CEO/IT Employee Provisioning Policy** – We attended the CEO/IT OCid meetings and provided feedback on CEO/IT's new policy on Employee Provisioning, which was developed in response to a prior external audit finding.
- 5. OC Public Works Franchise Fees** – The County receives about \$2.5 million annually in franchise fee revenue. OCPW requested our assistance in identifying potential audit firms specializing in franchise fee audits. We researched and provided OCPW with a list of potential franchise fee auditors along with sample reports. We also provided technical feedback on three quotes received by OCPW.
- 6. Human Resources RFP** – We participated as a member on the Evaluation Committee of the RFP for a Medical and Dental Claims Audit and Operational Assessment of the County's third party claims administrator.
- 7. John Wayne Airport Senior Quality Assurance Analyst Recruitment** – We assisted JWA in interviewing and evaluating a Senior Quality Assurance Analyst for its Airport Assurance & Compliance Unit.
- 8. Office of Protocol/International Visitors & Protocol Foundation of Orange County (IVPFOC)** – We provided several presentations to various foreign dignitaries in support of the IVPFOC's mission of promoting strong cultural, business and educational ties between the international community and Orange County governments and corporations.



REVENUE GENERATING LEASE AUDITS

The importance of the lease audits is underscored by the fact that in over a decade, the two agreements we audited in FY 10/11 will generate about \$43 million in revenue to the County.

We completed a total of 7 audits in this category as listed below.

Revenue Generating Lease Audits:

We completed **2** Audits of Revenue Generating Leases as listed below. In these audits, we determined if all revenues due to the County are properly calculated, recorded, and received. These audits are requested annually by John Wayne Airport (JWA), OC Dana Point Harbor Department (DPHD), OC Parks, and OC Public Works (OCPW).

The below two (2) lease/operating agreements generate approximately \$7 million annual gross receipts and \$4.3 million annual revenue to the County. The overarching purpose of the audits is to provide independent assurance that revenue due to the County is received in accordance with the agreements. As the average term of the agreements can range from 10 to 30 years, any additional revenue we identify will result in additional ongoing revenue over the life of the agreements. In addition, one of the below agreements is new. We also audited this agreement as a first time audit to help ensure the operator's accounting processes and records are on the "right track" and to make any necessary and timely corrections in the agreement terms.

- JWA – Valet Parking Services (Parking Concepts Inc.)
- OC Parks – Parking Services (Parking Concepts Inc.)

Follow-Up Audits for Revenue Generating Lease Audits:

We completed **5** First Follow-Up Audits as listed below:

First Follow-Up Audits:

- ▶ OC Public Works – Bella's Kitchen
- ▶ JWA – Budget Rent-A-Car
- ▶ OC Parks – Irvine Park Railroad
- ▶ OC Dana Point Harbor – Dolphin Safari
- ▶ OC Parks – Santiago Equestrian Center

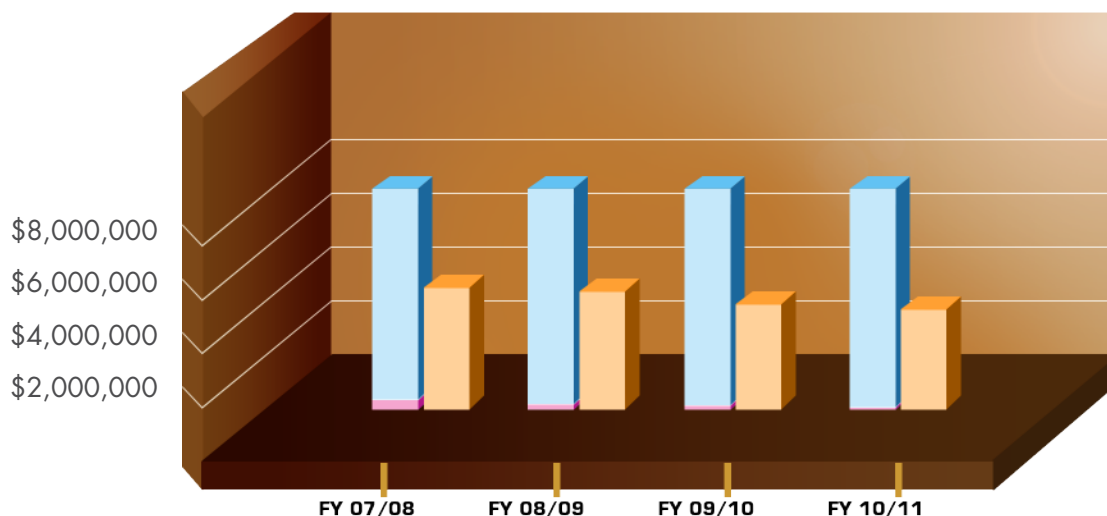




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■ ACTUAL AND POTENTIAL REVENUE RECOVERY



Dana Point Harbor Audit Added Revenue (2)	\$6,250,000	\$6,250,000	\$6,250,000	\$6,250,000
Other IAD Revenue Recoveries (1)	\$290,909	\$136,594	\$102,521	\$60,586
IAD Budget	\$2,973,741	\$2,916,012	\$2,526,955	\$2,659,188

(1) While not our predominant objective, the OC Internal Audit Department performs audits for revenue recoveries whenever the opportunity presents itself. We look for under-recovered revenues as a critical component of assisting management in safeguarding the County's assets. We conduct several audits of business contracted by agencies such as John Wayne Airport, OC Public Works, OC Parks, and the OC Dana Point Harbor to ensure all revenues due to the County are properly calculated and received. In addition, we perform monthly CAAT routines to determine if any duplicate payments to vendors have been mistakenly made.

As noted in prior year annual reports, for the past 4 years, average revenue recoveries represent **5.3%** of our annual budget excluding OC Dana Point Harbor, and over 200% including OC Dana Point Harbor.

OC DANA POINT HARBOR

(2) Our largest revenue recovery to date has been the Board of Supervisor's 2001 adoption of the Internal Audit Department's recommendation to retain Dana Point Harbor as a County-owned harbor operation. This decision is estimated to result in the County recovering, at a minimum, an additional \$250 million over 40 years on behalf of the taxpayers to be directly applied to continued enhancement of the harbor.

SPECIAL DISTRICT TAXES TO BE LOWERED BY \$20 MILLION

As a result of our audit of the Community Facility Districts (CFDs) – Ladera Ranch, the Special District (Mello-Roos) taxes for all 23 CFDs (6 in Ladera Ranch and 17 others) were lowered nearly \$20 million over the next three years. See more information about the audit on page 14.



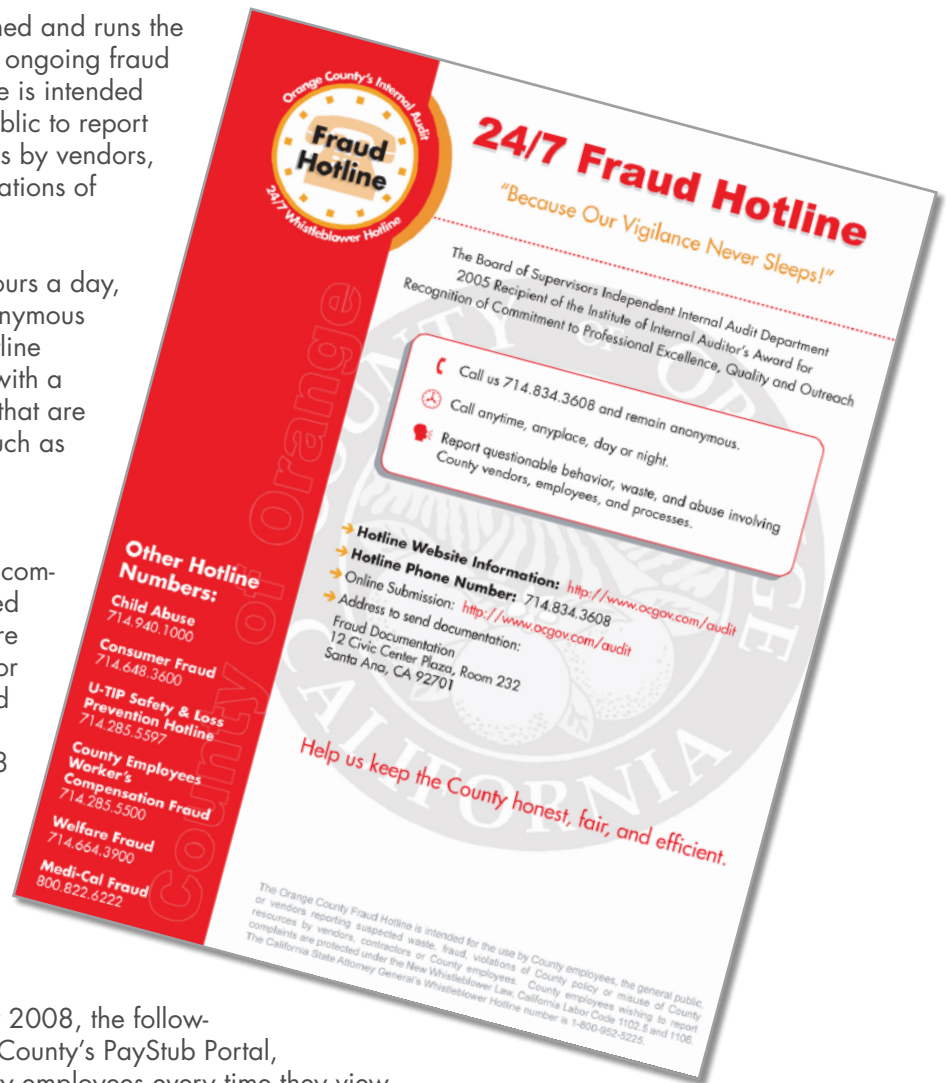
FRAUD HOTLINE

The OC Internal Audit Department established and runs the Orange County Fraud Hotline as part of its ongoing fraud detection and prevention effort. The Hotline is intended for County employees, vendors, and the public to report suspected fraud, misuse of County resources by vendors, contractors, or County employees, and violations of County policy.

The Hotline is monitored live for calls 24 hours a day, seven days a week. Callers can leave anonymous information or identify themselves. The Hotline telephone system also provides the callers with a list of Hotline numbers for reporting frauds that are not handled by the County Fraud Hotline such as Welfare Fraud.

In Fiscal Year 2010/2011, we saw a 9% increase in the number of Hotline incidents compared to the prior fiscal year. We processed **135 Hotline incidents**: 37 incidents were referred to County departments/agencies for investigation and 20 for their discretion and action, 55 incidents were referred to the Welfare Fraud Hotline for investigations, 18 were referred to outside agencies, and 5 were closed due to insufficient information. To date, three of the 37 incidents referred to County departments/agencies for investigation remain open.

Hotline Enhancements: Starting in July 2008, the following Fraud Hotline notice was added to the County's PayStub Portal, where it appears for all 18,000 plus County employees every time they view their pay checks (stubs) online. In addition, we coordinated with the County Executive Office to frequently post in the CEO's *County Connection* a notice for the Fraud Hotline.



ORANGE COUNTY'S INTERNAL AUDIT DEPARTMENT FRAUD HOTLINE

- If you suspect fraud, waste or abuse of County resources call the OC Internal Audit Department Fraud Hotline at (714) 834-3608.
- We take calls and e-mails 24/7.
Our site is <http://www.ocgov.com/audit>
- Call or email us anonymously and you will receive Whistleblower protection under California Law.



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Customer satisfaction surveys are sent to our clients when an audit is finalized and issued. These surveys measure the value of our audit services and report products. The customer satisfaction survey provides feedback regarding auditors' professionalism, timely communications, partnering, technical knowledge, and whether recommendations were practical and reasonable.

Customer Surveys on Audit Services Provided

4.5 on a scale of 5

Client satisfaction is also one of Internal Audit's Key Performance Measures in its Annual Business Plan. Our goal for FY 2010/11 was to obtain an average client satisfaction rating of "4" on a scale of 1 through 5. We are pleased to report our actual results for FY 2010/11 showed an average rating of 4.5, which demonstrates high client satisfaction with audit services.

Orange County
Internal Audit Department
Customer Survey of Audit Services

Name of Auditor(s):
Audit No.:
Name of Audit:

Please rate 1 to 5
1 being Strongly Disagree
5 being Strongly Agree
(The higher the score the better the evaluation)

Score	Evaluation Factors
1.	Were the auditor(s) professional and courteous?
2.	Did the auditor(s) communicate the objectives of the audit?
3.	Did the auditor(s) discuss findings with you in a timely manner?
4.	Did the auditor provide reasonable and practical recommendations?
5.	Was the audit report clear and accurate?
6.	Did the auditor(s) demonstrate satisfactory technical knowledge relating to internal control?
7.	Were your experiences with the auditor(s) positive?
8.	Would you recommend the services of the auditor(s) to your colleagues?

Items Not Addressed Above:

Customer Surveys & Client Satisfaction

Quotes from FY 2010/11 Customer Surveys:

"The audit team was extremely professional and courteous. They identified areas for improvement and offered suggestions and solutions." - **Office of the Public Defender**

"We appreciate that Internal Audit was flexible in discussing and updating a portion of one recommendation when we provided some additional information toward the end of the response period." - **OC Waste & Recycling**

"It was a good experience and there is no doubt that this will help to protect the County's interest." - **OC Public Works/OC Fleet Services**



AUDIT RECOMMENDATIONS

The OC Internal Audit Department tracks all audit recommendations made as of January 2003, including counts of audit recommendation, types of recommendations (e.g., material weakness/critical, significant weakness, control finding, or efficiency/effectiveness issue); management concurrence; implementation status of audit recommendations as determined in our Follow-Up Audits, and percentage of audit recommendations that were subject to follow-up.

OUTCOME

FY 2010/2011 Results

- **Recommendations Made: 122** recommendations were made in FY 10/11.
Types of Recommendations: Of the 122 recommendations made during FY 10/11, we identified **8 Critical Control Weaknesses/Material Weaknesses, 18 Significant Control Weaknesses and 96 Control Findings** including Compliance Issues and Efficiency or Effectiveness Issues.
- **Management Concurrence:** For each recommendation, management submits responses to Internal Audit that include their concurrence of audit findings and recommendations, implementation plans, and implementation dates. Of the **122** recommendations made during FY 10/11, **121 (99%) had full management concurrence, and 1 (1%) had partial management concurrence.**
- **Implementation Status:** Follow-Up Audits are performed at 6 months and, if necessary at 12 months, following the issuance of all final audit reports to verify the implementation status of audit recommendations. Because of the 6 and 12 month Follow-Up Audit periods, we do not have implementation status for all audits conducted in FY 2010/11.

Since 2003:

Recommendations Made:

Between January 2003 and June 2011, Internal Audit made **1,258** audit recommendations.

Types of Recommendations:

There were **9 Critical Control Weaknesses/Material Weaknesses (.7%), 68 Significant Control Weaknesses (5.4%), and 1,181 Control Findings (93.9%)** including Compliance Issues or Efficiency & Effectiveness Issues.

Management Acceptance/Concurrence:

Of the total 1,258 audit recommendations, we obtained **full or partial management concurrence on 99% of the recommendations.**

Implementation Status:

Follow-Up Audits are performed to verify the implementation status of audit recommendations. Since January 2003, we have followed-up on **974 audit recommendations.** Note: not all audit recommendations require follow-ups, and some are pending completion due to timing differences.

Of the 974 recommendations, **100% were verified as fully implemented and/or closed as follows:**

- **868** recommendations (**89%**) were implemented or closed by the First Follow-Up Audit.
- **106** recommendations (**11%**) were implemented or closed by the Second Follow-Up Audit.



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INTERNAL AUDIT DEPARTMENT PROFESSIONAL STAFF

Director of Internal Audit, Dr. Peter Hughes, Ph.D., MBA, **CPA**, CIA, CFE, CFF, CITP, CCEP
Deputy Director, Eli Littner, **CPA**, CIA, CFE, CFS, CISA

Senior Audit Manager, Michael J. Goodwin, **CPA**, CIA
Senior Audit Manager, Alan Marcum, MBA, **CPA**, CIA, CFE
Senior Audit Manager, Autumn McKinney, **CPA**, CIA, CISA, CGFM
Audit Manager, Lily Chin, **CPA**
IT Audit Manager, Wilson Crider, **CPA**, CISA, CICA
Audit Manager, Michael Dean, **CPA**, CIA, CCSA, CISA
Audit Manager, Winnie Y. Keung, **CPA**, CIA
Audit Manager, Carol L. Swe, **CPA**, CIA, CCSA, CISA
Audit Manager, Kenneth Wong, **CPA**, CIA
Senior Auditor, Lisette Free, **CPA**, CFE
Senior Auditor, Abdul Khan, **CPA**, CIA, CISA, CFS
Senior Auditor, Susan Nestor, **CPA**, CIA
Intern Auditor, Michael Steinhau

ADMINISTRATIVE STAFF

Administrative Manager, Renee Aragon
Staff Specialist/Deputy Purchasing Agent, Maribel Garcia

CERTIFICATION LEGEND

CPA
Certified Public
Accountant

CIA
Certified Internal
Auditor

CICA
Certified Internal
Controls Auditor

CCSA
Certification in Control
Self-Assessment

CISA
Certified Information
Systems Auditor

CFE
Certified Fraud
Examiner

CFF
Certified in Financial
Forensics

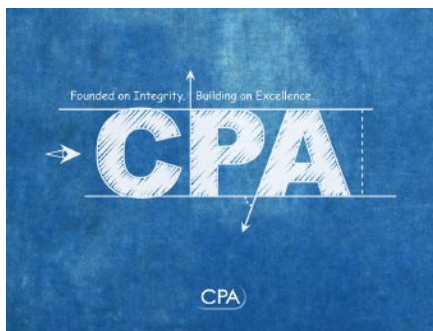
CFS
Certified Fraud
Specialist

CGFM
Certified Government
Financial Manager

CCEP
Certified Compliance
and Ethics Professional

CITP
Certified Information
Technology Professional

MBA
Masters in Business
Administration



STAFF TRAINING

Professional staff completed the minimum continuing professional education required for their professional licenses and certifications. Training was received in a variety of topics including government accounting and auditing standards updates, information technology auditing, and computer assisted audit techniques.



■ PROFESSIONAL CREDENTIALS

The OC Internal Audit Department is the only large county in the USA whose audit staff have the combination of **100% CPA's; 93% possessing double certifications; and 57% carrying three or more certifications.**

The OC Internal Audit Department follows the professional standards of the Institute of Internal Auditors (IIA), the U.S. Government Accountability Office (GAO), and the American Institute of Certified Public Accountants (AICPA), where applicable.

Accordingly, the Internal Audit Department and its individual auditors hold various professional licenses and certifications, and are members of many prestigious professional audit and accounting associations. At a minimum, each auditor is licensed as an active **Certified Public Accountant (CPA)**. See additional certifications on page 21 and related professional associations on pages 23 and 24.

WHY ARE CERTIFICATIONS AND PROFESSIONAL MEMBERSHIPS IMPORTANT?

Auditing and accounting related certifications and professional memberships are critical to our professional effectiveness for the following reasons:

- The certifications demonstrate a technical capability that is recognized internationally. The professional associations providing the certifications have rigorous standards and minimum requirements that include educational criteria, comprehensive written exams for technical knowledge and skills, and verified work experience.
- The certifications also have ethical requirements. These ethical requirements are important so that our judgment or professional opinions are not compromised.
- The memberships support our philosophy of continuous learning and improvement. Our membership and participation in professional associations allows us to be updated on relevant issues in business and industry with regard to accounting trends and developing best practices. Additionally, attendance at professional association conferences and meetings allow us to network and benchmark with our peers. Such constant renewal keeps us professionally current, refreshed, invigorated, and responsive to the County's needs.

Most importantly, possession of a CPA license and other relevant certifications allows us to assign qualified individuals to complex audits and makes us uniquely qualified within the County for our audit responsibilities.

For example, the Senior Audit Manager overseeing the OC Fraud Hotline, along with the Deputy Director and Director of Internal Audit are Certified Fraud Examiners. The Certified Fraud Examiner certification demonstrates our ability and qualification to oversee the OC Fraud Hotline and investigate, when necessary, allegations of theft, nepotism, defalcation, etc.



FY 2010/2011 INTERNAL AUDITOR'S ANNUAL REPORT



■ PROFESSIONAL ORGANIZATIONS



CALIFORNIA BOARD OF ACCOUNTANCY

The OC Internal Audit Department has the privilege of staffing **fourteen (14)** Certified Public Accountants (CPAs) licensed in the State of California and follows the guidelines of the (AICPA) American Institute of Certified Public Accountants.

AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS (AICPA)



DR. PETER HUGHES NAMED THE 2010 CPA OF THE YEAR FOR LOCAL GOVERNMENT

The American Institute of Certified Public Accountants is the national, professional association of Certified Public Accountants in the United States, with more than 360,000 members. Dr. Hughes attended the 2010 AICPA National Government Conference in August 2010 to receive his award.

GOVERNMENT PERFORMANCE AND ACCOUNTABILITY COMMITTEE (GPAC)

Dr. Hughes also is serving on the AICPA Government Performance and Accountability Committee (GPAC) for his first 3 year term. The GPAC represents CPAs working in all levels of federal, state, and local government and serves the public who depend on CPAs to help ensure government accountability.



CERTIFIED IN FINANCIAL FORENSICS

The American Institute of Certified Public Accountants (AICPA) established the Certified in Financial Forensics (CFF) in 2008 for CPAs who specialize in forensic accounting. The Internal Audit Department has **one** CFF.

THE INSTITUTE OF INTERNAL AUDITORS (IIA)

The OC Internal Audit Department has an annual sustaining membership with the Institute of Internal Auditors. **Eleven (11)** of our staff are Certified Internal Auditors (CIA) and **two** staff earned the Certification in Control Self-Assessment (CCSA).



THE INSTITUTE OF INTERNAL AUDITORS, RESEARCH FOUNDATION

Dr. Peter Hughes, Director of Internal Audit, served 5 terms (2005-2010) on the IIA's important Board of Research and Education for 2010-2011.



CALIFORNIA STATE ASSOCIATION OF COUNTIES (CSAC)

Dr. Hughes is recognized by CSAC as a designated authority regarding combating fraud in local government and was requested as a featured speaker at the California State Association of Counties (CSAC) Institute in Sacramento in October 2011.



ASSOCIATION OF CERTIFIED FRAUD EXAMINERS (ACFE)

The OCIAD has **four** staff that are Certified Fraud Examiners (CFE) and are members of the Association of Certified Fraud Examiners. Dr. Peter Hughes, Director of Internal Audit, served as a member of the ACFE's prestigious Editorial Advisory Committee. In 2009, Dr. Hughes was the recipient of the ACFE Outstanding Achievement Award – Hubbard Award for the prized article, "Ethics Pays in So Many Ways" published in 2008.





ASSOCIATION OF LOCAL GOVERNMENT AUDITORS (ALGA)

The OC Internal Audit Department has an annual sustaining membership with ALGA. Also, the OC Internal Audit Department published an article about OCIAD's CAAT routines and its use within Orange County in their Audit Abstracts Category of their quarterly publication. In 2008, the OC Internal Audit Department received the association's Bronze Website Award for our department website. IAD's article on CAATs was published in ALGA's Summer 2011 Quarterly Journal.



ASSOCIATION OF CERTIFIED FRAUD SPECIALISTS (ACFS)

The OC Internal Audit Department has **two** staff members that are a Certified Fraud Specialists. Dr. Peter Hughes, Director of Internal Audit, co-authored a five page article titled "Ethics Programs" that was published in the ACFS Fraud Magazine for July/August 2008.



CERTIFIED INFORMATION SYSTEMS AUDITORS (CISA) & INFORMATION SYSTEMS AUDIT AND CONTROL ASSOCIATION (ISACA)

The OC Internal Audit Department has **six** staff members who are Certified Information Systems Auditors (CISA) and are members of the Information Systems Audit and Control Association. Our IT Audit Manager developed and presented a training course about OCIAD's use of CAATs for the ISACA LA spring conference.



SOCIETY OF CORPORATE COMPLIANCE AND ETHICS (SCCE)

The OC Internal Audit Department has **one** staff member that is a Certified Compliance and Ethics Professional (CCEP).



GOVERNMENT FINANCE OFFICERS ASSOCIATION (GFOA)

The Government Finance Officers Association is to enhance and promote the professional management of governments for the public benefit by identifying and developing financial policies and best practices and promoting their use through education, training, facilitation of member networking, and leadership. Several of our staff are members of this organization.



CALIFORNIA COUNTIES AUDIT CHIEFS' COMMITTEE

The OC Internal Audit Department attends regular quarterly meetings and participates in the California Counties Audit Chief's Committee as part of the Peer Review Program. In June 2010, the OC Internal Audit Department received its fourth peer review and passed without exception.

CERTIFIED GOVERNMENT FINANCIAL MANAGER (CGFM) & ASSOCIATION OF GOVERNMENT ACCOUNTANTS (AGA)

The Internal Audit Department has **one** staff member who is a Certified Government Financial Manager (CGFM) and is a member of the Association of Government Accountants (AGA) organization.



■ THE YEAR AHEAD

APPROVAL OF FY 2011/12 AUDIT PLAN AND RISK ASSESSMENT

On April 27, 2011, the Audit Oversight Committee (AOC) approved the FY 2011/12 Audit Plan and Risk Assessment. This comprehensive report details our plan for audits and reviews in the upcoming fiscal year and incorporates the results of our extensive risk assessment. Any revisions or changes to the Audit Plan throughout the year are made in the OC Internal Audit Department's Quarterly Status Report and approved by the AOC.

BOARD OF SUPERVISORS AND AOC REQUEST FOR AUDITS

The OC Internal Audit Department reserves resources to accommodate Board of Supervisors requests. Board requests derive from Board-directed audits which require a Board majority vote of the Board, and specific audit projects asked for by a Supervisor's staff member. The Director of Internal Audit reserves the right to determine how to best fit audits and reviews directed by the Board and AOC into the Audit Plan.

FY 2011/12 AUDIT PLAN HIGHLIGHTS

■ Internal Control Audits

We will validate, substantiate, and confirm the integrity of internal controls over the following processes to ensure accurate, complete and timely processing of financial transactions and ensure County assets are safeguarded:

- ▶ **OC Public Works Fee Generated Revenues**
- ▶ **OC Public Works Flood Capital Projects**
- ▶ **John Wayne Airport Change Order/Contract Amendment Process**
- ▶ **Sheriff-Coroner Immigration & Customs Enforcement (ICE) Agreement**
- ▶ **Sheriff-Coroner Inmate Welfare Fund**
- ▶ **Probation GPS/Electronic Confinement Program Administration**
- ▶ **County General Fund Reserves/Cash Flow Operating Transfers**
- ▶ **OC Community Resources Disbursements Approval Process**
- ▶ **Social Services Agency Revolving Funds**
- ▶ **HCA Medical Billing**

■ Information Technology

The OC Internal Audit Department will provide internal controls assistance to the **PTMS Implementation and eProcurement solution**. We will focus specifically on the four control areas of segregation of duties; reviews and approvals; audit trails; and reconciliations. We also plan to provide IT audit assistance to selected Internal Control Audits.

We plan to perform IT audits of:

- ▶ **Auditor-Controller CAPS+HR/Payroll User Access/Segregation of Duties**
- ▶ **Social Services Agency General Control Review**
- ▶ **District Attorney General Control Review**
- ▶ **HCA Medical Billing – IRIS/Cerner System**

We will continue to perform computer assisted audit techniques (CAATs) of payroll and vendor payments.

■ Financial Audits and Mandates

In addition to our 5 **District Attorney Grant Audits**, we will conduct audits of **Treasurer-Tax Collector – Annual Investment Compliance Audit and the Tax Redemption Officer; CEO/Public Finance Community Facility Districts; and a Follow-Up Audit on CAFR/Single Audit Recommendations**.

■ Revenue Generating Lease Audits

Revenue generating lease audits ensure the correct amount of revenue is paid to the County based on a percentage of gross receipts. These critical audits are performed at the request of **John Wayne Airport, OC Public Works, OC Parks, and OC Dana Point Harbor**. The 3 lease audits scheduled this year have **combined annual revenue to the County of about \$1.7 million**.

OC Board of Supervisors' Internal Audit Department

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PROVIDING FACTS AND PERSPECTIVES COUNTYWIDE

TRANSPARENCY

The OC Internal Audit Department (OCIAD) reports directly to the Board of Supervisors on a monthly basis in a public forum. Additionally, the Internal Audit Department reports quarterly to the Board-appointed advisory group known as the Audit Oversight Committee. All final audit reports are available on the OCIAD website.

OCIAD MISSION

The mission of the OC Internal Audit Department is to provide reliable, independent, objective evaluations and business and financial advisory services to the Board of Supervisors and County management. Our role is to assist both parties with their important business and financial decisions; as well as, to contribute to protecting and safeguarding the County's resources and assets.

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